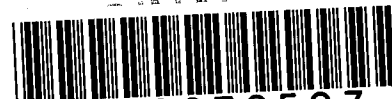


WILLIAM A. MUNDELL  
CHAIRMAN  
JIM IRVIN  
COMMISSIONER  
MARC SPITZER  
COMMISSIONER



0000039597

RECE

ARIZONA CORPORATION COMMISSION

2001 NOV -9 P 3:10

AZ CORP COMMISSION  
DOCUMENT CONTROL

Arizona Corporation Commission

DOCKETED

NOV 09 2001

DATE: NOVEMBER 9, 2001

DOCKET NO: E-02217A-01-0183

TO ALL PARTIES:

DOCKETED BY

*noe*

Enclosed please find the recommendation of Administrative Law Judge Lyn Farmer.  
The recommendation has been filed in the form of an Order on:

SALT RIVER PROJECT AGRICULTURAL IMPROVEMENT  
AND POWER DISTRICT  
(REVENUE BONDS)

Pursuant to A.A.C. R14-3-110(B), you may file exceptions to the recommendation of the Administrative Law Judge by filing an original and ten (10) copies of the exceptions with the Commission's Docket Control at the address listed below by 4:00 p.m. on or before:

NOVEMBER 19, 2001

The enclosed is NOT an order of the Commission, but a recommendation of the Administrative Law Judge to the Commissioners. Consideration of this matter has tentatively been scheduled for the Commission's Working Session and Open Meeting to be held on:

NOVEMBER 27, 2001 and NOVEMBER 28, 2001

For more information, you may contact Docket Control at (602)542-3477 or the Hearing Division at (602)542-4250.

BRIAN C. McNEIL  
EXECUTIVE SECRETARY

1 **BEFORE THE ARIZONA CORPORATION COMMISSION**

2 WILLIAM A. MUNDELL  
CHAIRMAN

3 JIM IRVIN  
COMMISSIONER

4 MARK SPITZER  
COMMISSIONER

5  
6 IN THE MATTER OF THE APPLICATION OF  
SALT RIVER PROJECT AGRICULTURAL  
7 IMPROVEMENT AND POWER DISTRICT FOR  
AN ORDER AUTHORIZING ITS ISSUANCE OF  
8 REVENUE BONDS AND REFUNDING  
REVENUE BONDS.

DOCKET NO. E-02217A-01-0183

**ORDER**

9 Open Meeting  
10 November 27 and 28, 2001  
Phoenix, Arizona

11 **BY THE COMMISSION:**

12 Having considered the entire record herein and being fully advised in the premises, the  
13 Arizona Corporation Commission ("Commission") finds, concludes, and orders that:

14 **FINDINGS OF FACT**

15 1. Salt River Project Agricultural Improvement and Power District ("SRP") is an  
16 agricultural improvement district duly organized and existing under Title 48, Chapter 17, Arizona  
17 Revised Statutes, and is a political subdivision of the State of Arizona pursuant to Article 13, Section  
18 7 of the Arizona Constitution.

19 2. SRP is principally engaged in the generation of electricity in the states of Arizona,  
20 New Mexico, Nevada and Colorado, and the purchase and sale of electricity to customers in  
21 Maricopa, Pinal and Gila Counties in Arizona. At the end of SRP's fiscal year ending April 30,  
22 2001, it served 746,386 customers.

23 3. SRP has three affiliated companies. New West Energy Corporation ("New West"),  
24 received a Certificate of Convenience and Necessity to provide competitive retail electric service in  
25 Arizona in Decision No. 61944 (September 17, 1999). New West markets SRP's surplus energy and  
26 provides other retail energy services, and SRP acts as a guarantor of New West's contractual  
27 obligations. Papago Park Center, Inc., another wholly-owned subsidiary of SRP, is engaged in land  
28 development, and the third affiliate, the Salt River Water Users' Association, is the predecessor of

1 SRP and operates and maintains the irrigation system of the Salt River Project as SRP's agent.

2 4. On March 1, 2001, SRP filed an application with the Commission for an order  
3 authorizing the issuance of up to \$500,000,000 in revenue bonds and up to \$550,000,000 in refunding  
4 bonds ("Application"). Pursuant to A.R.S. § 48-2465.B, SRP must secure "an order authorizing the  
5 issuance of such bonds in accordance with those provisions of § 40-302 pertaining to the issuance of  
6 bonds."

7 5. For the fiscal years 2001 through 2003, SRP expects to spend approximately \$1.1  
8 billion on capital items. Distribution plant is the largest category of expenditures and will require  
9 \$522.2 million of expenditures. Transmission, generation, competitive services, corporate services,  
10 and water operations will require \$596.7 million over the same period.

11 6. SRP intends to issue up to \$500.0 million in revenue bonds to finance distribution  
12 plant. Revenue bonds issued by an agricultural improvement district are secured by a pledge of and a  
13 lien on the revenues of its electric system, and the interest paid on the revenue bonds is not subject to  
14 income tax.

15 7. SRP also seeks authorization to issue up to \$550.0 million in refunding bonds  
16 associated with the \$500.0 million revenue bonds. Revenue bonds issued by SRP often have "call"  
17 features which allow for the redemption of a bond prior to its scheduled maturity. The decision to  
18 refund a specific bond depends upon the interest rates and call provisions on outstanding bonds,  
19 current market interest rates, the cost of funding an escrow, and other issuance costs. Using this  
20 analysis, the net present value savings for each issue is determined. According to SRP, historically, it  
21 has not refunded long maturity debt unless the debt service savings were 7.0 percent or greater, but  
22 has refunded shorter maturity debt with savings as low as 3.0 percent.

23 8. SRP's application includes a request for authorization to issue bond derivatives.<sup>1</sup>  
24 Bond derivatives are debt instruments that provide bondholders an income stream based on the  
25 market, rather than a coupon rate. The Commission granted SRP authority to issue derivatives for the  
26 first time in Decision No. 58386 (September 2, 1993) in order to provide SRP with the opportunity  
27

28 <sup>1</sup> Bond derivatives are also known as "alternative bond products".

1 for further debt service savings through the refunding process. The Commission restricted the  
2 issuance of derivatives to 7.0 percent of SRP's total capitalization, and in Decision No. 58625 (May  
3 2, 1994) continued to apply the 7.0 percent restriction. Currently, SRP has two types of alternative  
4 bond products. As part of its 1993 Series C bond sale, SRP issued \$36.7 million of Short Term  
5 Adjustable Rate Securities ("STARS") and \$36.7 million of Short Term Rate Inverse Payment  
6 Exempt Securities ("STRIPES"). The two derivative issues total slightly over 2.0 percent of SRP's  
7 total outstanding debt at the end of the most recent fiscal year. Staff recommends that SRP continue  
8 to have the ability to issue alternative debt instruments in a limited amount, with the total amount of  
9 derivatives to comprise no more than 7.0 percent of its total capitalization.

10 9. On June 11, 2001, SRP filed an amendment to the application ("Amended  
11 Application"), requesting approval of up to an additional \$175,000,000 in revenue bonds to refund  
12 commercial paper ("Commercial Paper Revenue Bonds") and up to an additional \$200,000,000 of  
13 associated refunding bonds. SRP currently has outstanding commercial paper in the amount of  
14 \$525.0 million, including \$150.0 million of Series A commercial paper, and \$375.0 million of Series  
15 B commercial paper<sup>2</sup>. In Decision No. 55209 (September 18, 1986) and Decision No. 56381 (March  
16 9, 1989), the Commission authorized SRP to issue up to \$425.0 million of revenue bonds to retire the  
17 Series B commercial paper. With this amended application, SRP seeks authority to issue revenue  
18 bonds to retire the Series A commercial paper, and corresponding authority to issue refunding  
19 revenue bonds.

20 10. According to the Staff Report, SRP's financial statements reflect continued strong  
21 financial health. SRP's capital structure has strengthened, with long-term debt falling from 63.0  
22 percent of its capital structure in 1999, to 57.3 percent in 2001. SRP's debt service coverage ratios  
23 have also increased during the same time period, from 3.20 in 1999, to 4.72 in 2001. In December,  
24 2000, Moody's Investor Service, Municipal Credit Research, Public Power, published an analysis of  
25

---

26 <sup>2</sup> The proceeds from the Series B commercial paper were used to refund prior notes that were issued, in part, to finance  
27 additions, improvements, and replacements to SRP's electrical power generation, transmission, distribution, and related  
28 facilities; finance a portion of the fuel inventory; and refund debt incurred under bank lines of credit. The proceeds from  
the Series A commercial paper were used to retire an equivalent amount of revenue bonds.

1 SRP's financial health and credit strength, stating that "[t]he Salt River Project's Aa2 rating and  
 2 positive outlook rests on its strong financial position, competitive rates, diverse power mix, and a  
 3 history of stable management . . . ." Staff notes that SRP's cash position at the end of the 2000-2001  
 4 fiscal year totaled close to \$1.0 billion.

5 11. In its Staff Report, Staff expresses concerns that the new debt will be allocated solely  
 6 to distribution assets. Staff also discusses how SRP's plan to enact a new master bond resolution and  
 7 recapitalize its debt ("Recapitalization Plan") would significantly increase the amount of debt  
 8 attributed to distribution. In the past, the allocation of SRP's debt proceeds to the various distribution,  
 9 generation, and transmission functions was inconsequential because all were included under one rate.  
 10 With the advent of electric competition and the effect of rate unbundling on customer retention, the  
 11 allocation of debt solely to the distribution function could have an affect on rates to distribution  
 12 customers. This is because the cash requirements of the distribution business would be  
 13 disproportionately higher than the cash requirements of the more competitive sectors of SRP's  
 14 business. If distribution rates reflected this allocation, distribution customers would have no  
 15 alternative provider, as distribution service is not subject to competition.

16 12. According to the Staff Report, SRP assured Staff that it has no plans to divest  
 17 generation or transmission, and that for accounting purposes, issuance purposes and rate setting, it  
 18 will continue to spread the debt balances among the three functions.<sup>3</sup> SRP has also assured Staff that  
 19 the allocation or "attribution" of debt for income tax purposes will not be adopted for ratemaking.  
 20 Further, pursuant to A.R.S. § 40-302.C, our approval of SRP's financing requests restrict SRP to use  
 21 the proceeds for the purposes set forth in Orders.

22 13. On September 12, 2001, the Commission's Utilities Division Staff ("Staff") issued its  
 23 Staff Report recommending approval of the Amended Application without a hearing, with the  
 24 following conditions:

- 25 a. bond derivatives and alternative bond products should be limited to 7.0  
percent of SRP's capital structure;
- 26 b. SRP file a report including the date of issuance, interest rate, maturity,  
27 the amount of discount or premium and issuance expenses, within two  
weeks after the issuance of any bonds authorized by this Decision; and

28 <sup>3</sup> For income tax purposes, SRP will "attribute" the new bond proceeds solely to distribution plant.

- 1 c. SRP file a report showing the savings to be experienced from the  
2 issuance of refunding bonds authorized by this Decision, within two  
3 weeks after issuance of the refunding bonds.

4 Staff believes that with the above conditions, pursuant to A.R.S. § 40-302, the debt issuance is  
5 reasonably necessary and appropriate for the purposes specified in the application and that such  
6 purposes are not reasonably chargeable to operating expenses or to income.

### 7 CONCLUSIONS OF LAW

8 1. The Commission has jurisdiction over the Application pursuant to A.R.S. §§ 40-302  
9 and 48-2465.B.

10 2. The proposed issuance by SRP of the revenue bonds and the refunding revenue bonds  
11 as requested in the Amended Application is within the powers of SRP as an agricultural improvement  
12 district pursuant to A.R.S. §48-2471 and is compatible with the public interest.

13 3. The revenue and refunding bonding authority approved herein is for the purposes  
14 stated in the application and is reasonably necessary for those purposes, and such purposes are not,  
15 wholly or in part, reasonably chargeable to operating expenses or to income.

16 4. Notice of the application was given in accordance with the law.

### 17 ORDER

18 IT IS THEREFORE ORDERED that the Application of Salt River Project Agricultural  
19 Improvement and Power District for authorization to issue an amount not to exceed \$500,000,000 of  
20 revenue bonds for construction purposes and for authorization to issue an amount not to exceed  
21 \$550,000,000 of associated refunding revenue bonds as described herein is hereby approved subject  
22 to the conditions set forth herein.

23 IT IS FURTHER ORDERED that the Application of Salt River Project Agricultural  
24 Improvement and Power District for authorization to issue an amount not to exceed \$175,000,000 of  
25 revenue bonds for the purpose of retiring Series A Commercial Paper and for authorization to issue  
26 an amount not to exceed \$200,000,000 of associated refunding revenue bonds as described herein is  
27 hereby approved subject to the conditions set forth herein.

28 IT IS FURTHER ORDERED that the authorization granted herein is expressly conditioned  
upon the application by Salt River Project Agricultural Improvement and Power District of the

1 proceeds derived thereby for those purposes set forth in the Application.

2 IT IS FURTHER ORDERED that Salt River Project Agricultural Improvement and Power  
3 District shall be authorized to take any and all steps necessary to effectuate the authorization herein.

4 IT IS FURTHER ORDERED that the total amount of derivatives or other alternative bond  
5 products issued by Salt River Project Agricultural Improvement and Power District shall not exceed  
6 seven percent of its total capitalization.

7 IT IS FURTHER ORDERED that Salt River Project Agricultural Improvement and Power  
8 District shall file with the Commission a report including the date of issuance, interest rate, maturity,  
9 the amount of discount or premium, and issuance expenses within two weeks after the issuance of  
10 any revenue bonds authorized by this Decision.

11 ...

12 ...

13 ...

14 ...

15 ...

16 ...

17 ...

18 ...

19 ...

20 ...

21 ...

22 ...

23 ...

24 ...

25 ...

26 ...

27 ...

28 ...

1 IT IS FURTHER ORDERED that Salt River Project Agricultural Improvement and Power  
2 District shall file with the Commission a report with an analysis showing the savings to be  
3 experienced from issuance of any refunding bonds authorized by this Decision, within two weeks of  
4 issuance of such refunding bonds.

5 IT IS FURTHER ORDERED that this Decision shall become effective immediately.

6 BY ORDER OF THE ARIZONA CORPORATION COMMISSION.

7  
8  
9 CHAIRMAN COMMISSIONER COMMISSIONER

10  
11  
12 IN WITNESS WHEREOF, I, BRIAN C. McNEIL, Executive  
13 Secretary of the Arizona Corporation Commission, have  
14 hereunto set my hand and caused the official seal of the  
Commission to be affixed at the Capitol, in the City of Phoenix,  
this \_\_\_\_ day of \_\_\_\_, 2001.

15  
16 BRIAN C. McNEIL  
EXECUTIVE SECRETARY

17  
18 DISSENT \_\_\_\_\_  
19 LAF:dap



1 SERVICE LIST FOR:

SALT RIVER PROJECT AGRICULTURAL  
IMPROVEMENT AND POWER DISTRICT

2  
3 DOCKET NO.:

E-02177A-01-0183

4 W. Gary Hull

Jane D. Alfano

5 SALT RIVER PROJECT AGRICULTURAL IMPROVEMENT  
AND POWER DISTRICT

6 P.O. Box 52025, PAB 207

7 Phoenix, Arizona 85072-2025

8 Kenneth C. Sundlof

JENNINGS, STROUSS & SALMON, P.L.C.

9 One Renaissance Square

Two N. Central Avenue

10 Phoenix, Arizona 85004-2393

11 Christopher Kempley, Chief Counsel

Legal Division

ARIZONA CORPORATION COMMISSION

12 1200 West Washington Street

13 Phoenix, Arizona 85007

14 Ernest G. Johnson, Director

Utilities Division

ARIZONA CORPORATION COMMISSION

15 1200 West Washington Street

16 Phoenix, Arizona 85007